

Audit Report



COMPILATION OF THE FY 2000 NAVY WORKING CAPITAL FUND FINANCIAL STATEMENTS

Report No. D-2001-155

July 3, 2001

Office of the Inspector General
Department of Defense

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Abstract We performed this audit in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, which requires DoD to provide audited financial statements to the Office of Management and Budget. This is the fifth and final report on our audit work on the FY 2000 Navy Working Capital Fund Financial Statements and related controls and supporting financial data. The previous reports dealt with inventory valuation, problems with a financial feeder system, intragovernmental transactions, and our endorsement of the Naval Audit Service disclaimer of opinion on the financial statements. These reports are listed in Appendix A. The Defense Finance and Accounting Service (DFAS) provides finance and accounting support, maintains the official accounting records, and prepares the financial statements using data from supporting field offices. The FY 2000 Navy Working Capital Fund Financial Statements reported total assets of \$25.1 billion and total liabilities of \$6 billion as of September 30, 2000. Also, the FY 2000 financial statements showed earned revenue of \$13.7 billion and program costs of \$13.6 billion.		
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Acronyms

CDB	Central Data Base
DBMS	Defense Business Management System
DDRS	Defense Departmental Reporting System
DFAS	Defense Finance and Accounting Service
IG	Inspector General
JV	Journal Voucher
USGSGL	U.S. Government Standard General Ledger
WCF	Working Capital Fund



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
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July 3, 2001

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE

SUBJECT: Audit Report on Compilation of the FY 2000 Navy Working Capital Fund
Financial Statements (Report No. D-2001-155)

We are providing this report for your review and comment. We conducted the audit in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. We considered management comments on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Comments were not fully responsive. Therefore we request that management provide additional comments on Recommendations B.1. and B.2. by August 3, 2001.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Marvin L. Peek at (703) 604-9587 (DSN 664-9587) (mpeek@dodig.osd.mil) or Mr. Joel K. Chaney at (216) 522-6091 (DSN 580-6091), extension 235 (jchaney@dodig.osd.mil). See Appendix B for the report distribution. The audit team members are listed inside the back cover.


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Office of the Inspector General, DoD

Report No. D-2001-155

(Project No. D2000FC-0279.004)

July 3, 2001

Compilation of the FY 2000 Navy Working Capital Fund Financial Statements

Executive Summary

Introduction. We performed this audit in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, which requires DoD to provide audited financial statements to the Office of Management and Budget. This is the fifth and final report on our audit work on the FY 2000 Navy Working Capital Fund Financial Statements and related controls and supporting financial data. The previous reports dealt with inventory valuation, problems with a financial feeder system, intragovernmental transactions, and our endorsement of the Naval Audit Service disclaimer of opinion on the financial statements. These reports are listed in Appendix A. The Defense Finance and Accounting Service (DFAS) provides finance and accounting support, maintains the official accounting records, and prepares the financial statements using data from supporting field offices. The FY 2000 Navy Working Capital Fund Financial Statements reported total assets of \$25.1 billion and total liabilities of \$6 billion as of September 30, 2000. Also, the FY 2000 financial statements showed earned revenue of \$13.7 billion and program costs of \$13.6 billion.

Objectives. The overall audit objective was to determine the reliability and effectiveness of processes and procedures used to compile and prepare the FY 2000 Navy Working Capital Fund Financial Statements. We reviewed DFAS Cleveland processes for consolidating and summarizing financial data from Navy Working Capital Fund field organizations. We also reviewed DFAS Cleveland processes and procedures for recording journal vouchers to adjust accounting data provided by Navy Working Capital Fund field organizations, DFAS accounting offices and other sources. In addition, we reviewed management controls and compliance with laws and regulations as they related to the audit objective.

Results. DFAS Cleveland and Kansas City recorded 974 departmental-level journal vouchers, valued at \$947.3 billion, that affected the FY 2000 financial statements. Review of 658 journal vouchers showed that 432 journal vouchers, valued at \$885.9 billion, were supported or proper. A prior report addressed 95 of 151 journal vouchers, valued at \$28.8 billion, related to intragovernmental transactions that were not adequately supported.

Of the remaining 507 journal vouchers reviewed, 70 journal vouchers, valued at \$19.4 billion, were unsupported. Although DFAS personnel provided adequate supporting documentation in some cases up to 42 days after we requested the information, current DFAS guidance requires supporting documentation to be available within 5 workdays after the journal vouchers are approved. Also 61 journal vouchers,

valued at \$10.7 billion, were out of balance because of interface and incompatibility problems with feeder systems. As a result, we could not rely on data created by unsupported journal vouchers and DFAS personnel were required to adjust data unnecessarily to enter data from legacy accounting feeder systems. Recording unsupported journal vouchers adversely affected the reliability of the FY 2000 financial statements (finding A).

DFAS Cleveland did not adequately document the audit trail from the ending trial balance in the Central Data Base to the opening trial balance in the Defense Departmental Reporting System. Adjustments of \$5.9 billion were made for financial reporting purposes. The adjustments were not sufficiently documented to permit tracing amounts from the source data within the Central Data Base to amounts reported on the financial statements by the Defense Departmental Reporting System. As a result, the inadequately documented transition made it difficult to verify that the calculations were consistently made (finding B).

Summary of Recommendations. We recommend that DFAS comply with guidance for recording Centralized Expenditure and Reimbursement Processing System balances, both inception to date and current year balances, in the activity general ledgers and reconciling any differences; require accounting personnel to provide adequate supporting documentation for all journal vouchers; import the Central Data Base trial balance to the Defense Departmental Reporting System without modification; develop standard operating procedures and documentation for adjusting accumulated operating results and record those adjustments in the Defense Departmental Reporting System; and improve crosswalks and complete documentation for populating budgetary information in the Defense Departmental Reporting System.

Management Comments. DFAS generally concurred with all recommendations except the recommendations to import trial balance data directly into the Defense Departmental Reporting Systems and record all adjustments to the trial balance using journal vouchers to the Defense Departmental Reporting System. DFAS indicated that adequate audit trails for the differences exist in offline spreadsheets. Although DFAS concurred with the recommendation to provide adequate support for all journal vouchers, it stated that adequate documentation for the journal vouchers existed. See the Finding section of the report for a discussion of the management comments and the Management Comments section of the report for the complete text of the comments.

Audit Response. We considered management comments responsive except for the statement that offline spreadsheets rather than journal vouchers are a sufficient audit trail to support changes between the Central Data Base and the Defense Departmental Reporting System. We believe that any adjustment of Navy Working Capital Fund financial information after the Central Data Base closes should be recorded in the Defense Departmental Reporting System as a journal voucher and subjected to the internal controls provided by that process. We request that DFAS reconsider its position and provide additional comments to the final report by August 3, 2001.

Table of Contents

Executive Summary	i
Introduction	
Background	1
Objectives	2
Findings	
A. Journal Vouchers	3
B. Audit Trails	12
Appendices	
A. Audit Process	
Scope	16
Methodology	17
Management Control Program Review	18
Prior Coverage	18
B. Report Distribution	20
Management Comments	
Defense Finance and Accounting Service	23

Background

The audit was performed as part of our efforts to meet the requirements of Public Law 101-576, the "Chief Financial Officers Act of 1990," November 15, 1990, as amended by Public Law 103-356, the "Federal Financial Management Act of 1994," October 13, 1994. This report is the fifth and final in a series of reports on the FY 2000 Navy Working Capital Fund Financial Statements and related controls and supporting financial data. The previous reports dealt with inventory valuation, problems with a financial feeder system, intragovernmental transactions, and our endorsement of the Naval Audit Service disclaimer of opinion on the FY 2000 Navy Working Capital Fund Financial Statements. See Prior Coverage in Appendix A for a listing of the prior reports. This part of our audit focused on the Defense Finance and Accounting Service (DFAS) Cleveland processes and procedures to compile financial data received from Navy field organizations and other sources to prepare the FY 2000 Navy Working Capital Fund Financial Statements.

Navy Working Capital Fund. The Navy Working Capital Fund (WCF) finances six primary activity groups, which provide support to the Navy and other authorized customers: Depot Maintenance, Transportation, Base Support, Information Services, Research and Development, and Supply Management. All of the primary activity groups except Supply Management are often referred to as the Industrial Fund business area. The FY 2000 Navy Working Capital Fund Financial Statements reported \$25.1 billion in assets, \$6 billion in liabilities, \$13.7 billion in earned revenue, and \$13.6 billion in program costs.

DFAS Responsibilities. DFAS Cleveland performs accounting functions and prepares the financial statements for the Navy WCF. Each month, DFAS Cleveland received financial information in various forms from Navy WCF field organizations, DFAS accounting offices, and other organizations, and recorded the data into the Central Data Base (CDB) accounting system. DFAS Cleveland consolidated the financial data for each activity group and prepared both the monthly reports and annual financial statements for the Navy WCF. As part of the compilation process, DFAS Cleveland recorded JVs in the CDB and in offline financial reporting systems.

Preparation of the Navy Working Capital Fund Financial Statements. At the end of FY 2000, DFAS Cleveland departmental accounting personnel performed the month-end processing functions and produced both the monthly reports and ending trial balance from the CDB system. General ledger accounts used for the CDB trial balance were then converted, or crosswalked, by DFAS Cleveland personnel into U.S. Government Standard General Ledger (USGSGL) format.¹ In cases where the CDB trial balance could not be directly crosswalked into a USGSGL account, DFAS Cleveland departmental accounting personnel computed the values for certain USGSGL general ledger accounts using offline spreadsheets. The adjusted trial balance in USGSGL format was then uploaded into the Defense Departmental Reporting System (DDRS). DDRS is a software

¹General ledger accounts in the CDB were converted to the USGSGL at the beginning of FY 2001. This should reduce the number of crosswalks that were required in prior years.

application created during FY 2000, which was used to document ending trial balances from other accounting systems and adjustments necessary to produce a final trial balance used to prepare the annual financial statements.

Objectives

The overall audit objective was to determine the reliability and effectiveness of processes and procedures used to compile and prepare the FY 2000 Navy Working Capital Fund Financial Statements. We reviewed DFAS Cleveland processes for consolidating and summarizing financial data from Navy WCF field organizations. We also reviewed DFAS Cleveland processes and procedures for recording JVs to adjust accounting data provided by Navy WCF field organizations, DFAS accounting offices and other sources. In addition, we reviewed management controls and compliance with laws and regulations as they related to the audit objective. See Appendix A for a discussion of the audit process and DFAS Cleveland management control program.

A. Journal Vouchers

DFAS Cleveland and Kansas City recorded 974 departmental-level journal vouchers (JVs), valued at \$947.3 billion, that impacted amounts reported on the FY 2000 Navy Working Capital Fund Financial Statements.

- 173 JVs, valued at \$37.5 billion, were related to intragovernmental transactions. Review of 151 of those JVs, valued at \$37 billion, showed that 95 JVs, valued at \$28.8 billion, were not adequately supported. JVs and other issues related to identifying and recording intragovernmental transactions were discussed in a prior report.²
- Of the remaining 801 JVs, review of 507 JVs, valued at \$907.8 billion, showed that 376 JVs, valued at \$877.7 billion, were supported, 70 JVs, valued at \$19.4 billion, were unsupported, and 61 JVs, valued at \$10.7 billion, were out of balance.

Incomplete documentation for the JVs occurred because DFAS Cleveland personnel did not always comply with DoD guidance and supporting accounting offices did not perform required reconciliations. DFAS Cleveland personnel recorded 61 JVs that were out of balance in order to correct errors caused by legacy³ DFAS feeder systems that produced data that was incompatible with the CDB and to correct errors caused by crosswalk problems. As a result, we could not rely on data created by unsupported JVs, and DFAS personnel were required to manipulate data unnecessarily to enter data from legacy accounting feeder systems. Unsupported JVs adversely affected the reliability of the FY 2000 Navy Working Capital Fund Financial Statements.

Guidance for Preparing Journal Vouchers

DoD Regulation 7000.14-R, “DoD Financial Management Regulation,” volume 6, “Reporting Policies and Procedures,” February 12, 1996, requires DFAS to establish procedures to ensure that the preparation of financial statements is timely and auditable and that controls are in place to provide accurate and complete statements. The regulation states that DFAS should adequately support and justify in writing any adjustment to the official accounting records. The regulation also provides that the documentation of JVs should be detailed enough to provide an audit trail.

² The adequacy and supporting documentation for these JVs is discussed in Inspector General (IG), DoD, Report No. D-2001-139, “Compiling and Reporting FY 2000 Navy Working Capital Fund Intragovernmental Transactions,” June 18, 2001.

³A “legacy” accounting system does not comply with Federal accounting standards and will be replaced with a compliant system in the future. DoD prohibits funding major improvements to legacy systems.

DFAS Director for Accounting memorandum, "Journal Voucher Guidance," August 2, 2000, provides additional guidance for JVs. The memorandum prescribes operational internal controls for JV processing. It categorizes JVs by type and establishes specific documentation requirements for support of each adjustment type. Supervisory approval requirements are established based on the dollar value of the JV. All required supporting documentation must be identified and made available no more than 5 workdays after a JV is approved. In addition, JVs may be recorded based on summary-level collection and disbursement data. The support required for that type of transaction consists of the summarized collection and disbursement amounts. However, for audit trail purposes, the detailed transaction-level amounts are to be obtained from the transmittal source, when it becomes available.

Summary of Departmental-Level Journal Vouchers Recorded

DFAS Cleveland and Kansas City recorded 974 departmental-level JVs, valued at \$947.3 billion, in FY 2000. There were 173 JVs, valued at \$37.5 billion, related to intragovernmental transactions. Our review of 151 of 173 JVs is discussed in IG, DoD, Report No. D-2001-139, June 18, 2001. Results of our review of the remaining 801 JVs, valued at \$909.8 billion, are discussed in this report. Of the 801 JVs, DFAS Cleveland and Kansas City did not adequately support 70 JVs, valued at \$19.4 billion; and 61 JVs, valued at \$10.7 billion, were out of balance. The following table summarizes the results of our review.

FY 2000 Departmental-Level Journal Vouchers (dollars in billions)					
JV Type	Supported (JVs)	Unsupported (JVs)	Out of Balance (Improper ¹) (JVs)	Not Reviewed (JVs)	Total (JVs)
JVs in CDB					
Redistribution	--	\$17.0 (26)	--	--	\$17.0 (26)
Undistributed Disbursements and Collections	--	\$2.0 (33)	--	--	\$ 2.0 (33)
System Interface Problems	--	--	\$ 9.6 ² (55)	--	\$ 9.6 (55)
Other	\$154.0 (256)	\$0.4 (4)	\$ 0.2 ² (4)	\$ 2.0 (294)	\$156.6 (558)
JVs for Cost of Goods Sold Model	\$720.5 (22)	--	\$ 0.9 (2)	--	\$721.4 (24)
JVs in DDRS					
Cleveland	\$3.1 (87)	--	--	--	\$3.1 (87)
Kansas City	\$0.05 (11)	\$0.05 (7)	--	--	\$ 0.1 (18)
Subtotal (discussed in this report)	\$877.7 (376)	\$19.4 (70)	\$10.7 (61)	\$2.0 (294)	\$909.8 (801)
JVs for Intragovernmental Transactions³	\$8.2 (56)	\$28.8 (95)	--	\$0.5 (22)	\$37.5 (173)
Total Navy WCF	\$885.9 (432)	\$48.2 (165)	\$10.7 (61)	\$2.5 (316)	\$947.3 (974)

¹These JVs were needed to correct out of balance conditions caused by feeder systems that provided incompatible data with the CDB. Because the JVs did not balance, they were included in our report on DoD-Wide Financial Statements IG, DoD, Report No. D-2001-070.

²The dollar values of out of balance JVs in the narrative are slightly different than the table due to rounding and the need to match the unsupported entries with the \$10.7 billion total shown in the table. The \$10.7 billion total for out of balance JVs was calculated based on JVs with debits of \$9.8 billion posted in the CDB (credits were \$9.3 billion) plus a one-sided credit entry to the Cost of Goods Sold model of \$0.9 billion.

³These entries are discussed in a separate report on intragovernmental transactions, IG, DoD, Report No. D-2001-139.

Unsupported Journal Vouchers

DFAS Cleveland and Kansas City recorded 70 JVs in support of the FY 2000 financial statements, valued at \$19.4 billion, which were not adequately supported. DFAS personnel were able to provide supporting documentation in some cases after we determined that support was inadequate. However, these JVs were considered as unsupported because DFAS guidance requires that all supporting documentation be available no later than 5 workdays after a JV is approved, which could be several months prior to the date that auditors review a JV package for adequate supporting documentation.

Redistribution of Funds Disbursed. Of the 70 unsupported JVs, 26 JVs, valued at \$17 billion, were recorded to redistribute Funds Disbursed - Other than Automatic Reimbursement Program (general ledger account No. 10122) between organizations for Supply Management, Budget Projects 91 and 92. The JVs did not contain sufficient information to evaluate the purpose of the adjustment or sufficient documentation of how the adjustment amount was calculated. DFAS Cleveland officials agreed that documentation supporting the JVs was incomplete. DFAS Cleveland provided a satisfactory written explanation of the system problem requiring the adjustments to be made; however, that information was not provided until 42 days after we informed them of the need for additional information.

JVs to Record Undistributed Collections and Disbursements. Of the 70 unsupported JVs, DFAS Cleveland personnel recorded 33 JVs, valued at \$2 billion, to reconcile or record values related to undistributed transactions.

Adjustments for Unreconciled Amounts from Navy WCF Field Organizations. DFAS personnel recorded 19 of the 33 unsupported JVs, valued at \$1.4 billion, based on summary-level financial data. DFAS Cleveland personnel needed to record these summary-level adjustments for 17 of the 46 field organizations in the Industrial Fund business area because DFAS accounting offices at Charleston, Columbus, Norfolk, Pensacola, and Oakland supporting DFAS Cleveland did not adjust inception to date and year to date collections and disbursements to agree with the Centralized Expenditure and Reimbursement Processing System. The calculations represented the difference between collections and disbursements recorded in the general ledger accounts for Industrial Fund organizations and the collection and disbursement values in the Centralized Expenditure and Reimbursement Processing System. DoD Regulation 7000.14-R, volume 4, requires that cash receipts and disbursements should be reconciled with appropriate documents and accounting records, as applicable within each accounting period.

Allocation of Undistributed Collections. DFAS personnel recorded 13 of the 33 JVs, valued at \$509 million, to allocate undistributed collections between intragovernmental and non-Federal. An allocation was needed because DFAS Cleveland did not have the detailed transactions comprising the undistributed collections that would provide the correct allocation. The allocation applied 79 percent of the undistributed collections to intragovernmental and 21 percent to non-Federal. This allocation was made

because the DFAS Director of Accounting directed that undistributed collections be recorded against accounts receivable for the financial statement presentation. The documentation accompanying the JV did not identify the purpose of the allocation or the basis for the allocation ratios. Subsequent to our analysis, DFAS Cleveland was able to provide additional documentation to support their actions 42 days after we requested the information. However, the inability of accounting systems to provide the required data forced DFAS to make the unsupported JVs.

Undistributed Collections and Disbursements for Navy Component. One of the 33 JVs, valued at \$49 million, was recorded in the Navy Component business area⁴ of the CDB to account for the differences between undistributed collections and disbursements reported to the U.S. Treasury for the Navy WCF that were not identifiable to a specific Navy WCF activity group. Component business area undistributed collections and disbursements represented the difference between all Navy WCF activity group balances and the Navy WCF total in the Centralized Expenditure and Reimbursement Processing System. This adjustment was unsupported because the detailed transactions for the general ledger values were not available from the Centralized Expenditure and Reimbursement Processing System. The DFAS Cleveland plan to remedy the undistributed collection and disbursement problems, scheduled for completion by September 2001, involves the creation and implementation of reconciliation procedures and the monitoring of the reconciliations on a monthly basis. We are not making recommendations pending the outcome of the DFAS initiatives.

Other Unsupported JVs. DFAS personnel recorded four JVs, valued at \$374 million, to the CDB, for which the supporting documentation accompanying the JV did not provide sufficient information to evaluate the entry. During subsequent meetings, DFAS Cleveland officials agreed that documentation supporting the JVs was incomplete and 7 days after we requested the information, provided additional support, which documented the entries.

JVs in DDRS by DFAS Kansas City. DFAS Kansas City recorded the remaining 7 of the 70 JVs in DDRS, valued at \$55 million, that were unsupported. DFAS Kansas City did not provide adequate descriptions explaining the purpose of the entries or documentation supporting the amount of the entry. For example, two JVs, valued at \$36.8 million, were recorded to adjust contract authority to reconcile with the annual Year-End Closing Statement (FMS 2108) report. However, no documentation was provided to show how the reconciliation was performed.

Out of Balance Journal Vouchers

DFAS Cleveland recorded 61 JVs, valued at \$10.7 billion, that were out of balance (because debits did not equal credits). The principal purpose of the JVs was to correct errors that occurred when data from other DFAS and Navy

⁴The Component business area is not an operational activity unit or group within the CDB, but is rather an administrative reporting mechanism used to reflect transactions (primarily collections and disbursements) that are not readily identifiable with a single activity or activity group.

accounting systems were initially recorded in the CDB or when data from the CDB were recorded in the Cost of Goods Sold model.⁵ Therefore, the out of balance (improper) JVs were necessary.

JVs Required to Correct Accounting System and Interface Problems.

DFAS Cleveland recorded 55 JVs, valued at \$9.6 billion, that were out of balance, to correct imbalances created when financial data from the Defense Business Management System (DBMS) and Material Financial Control System were uploaded into the CDB.

Defense Business Management System. Of the 55 JVs, 48 JVs, with debits valued at \$8.5 billion and credits valued at \$8.9 billion, were needed to correct errors that occurred when trial balances from the DBMS system were recorded in the CDB. IG, DoD, Report No. D-2000-140, “Compilation of the FY 1999 Department of the Navy Working Capital Fund Financial Statements,” June 7, 2000, recommended that DFAS modify DBMS to provide accounting data in a format that is compatible with accounting logic in the CDB. DFAS responded that changes would not be made to DBMS because it is a legacy system and that actions were underway to replace the DBMS with the Business Management Redesign system.

DBMS Accounting. DFAS Cleveland recorded 27 JVs with total debits of \$8.5 billion and total credits of \$8.9 billion to correct errors resulting from accounting differences between the DBMS and CDB. The DBMS did not close certain general ledger accounts at year’s end that are closed in the CDB. Inception-to-date amounts for those general ledger accounts based on the DBMS trial balance would cause out of balance conditions in the CDB and duplication of operating results. The DFAS Cleveland accounting entries prevented the errors caused by the accounting differences by restating general ledger balances at the beginning of the fiscal year.

DBMS Reporting. DFAS Cleveland recorded 21 JVs with debits valued at \$13.7 million and credits valued at \$3.4 million to correct errors that occurred because the DBMS reported accounting data in a format that was not compatible with the posting logic for the CDB and caused the CDB to be out of balance after DBMS balances were uploaded. When a transaction (total debits and total credits) was out of balance, DFAS departmental accounting personnel researched the conversion and posting of the DBMS data and recorded a one-sided accounting entry to correct the CDB balance.

Material Financial Control System. DFAS Cleveland recorded seven JVs to correct problems related to uploading financial data from the Material Financial Control System, a financial feeder system used by the Naval Supply Systems Command.

⁵The Under Secretary of Defense (Comptroller) and DFAS developed a Cost of Goods Sold model, which has been used since FY 1995, to revalue inventory from standard price to an estimation of historical cost for financial reporting. Use of the model requires numerous adjustments to several general ledger accounts. Both the auditors and DoD management agree that the model has serious flaws.

- Five one-sided JVs, valued at \$1.1 billion, were needed to correct an out of balance condition that occurred because the posting logic was not correct.
- Two one-sided JVs, valued at \$166,000, were needed to correct erroneous transactions recorded in prior years that caused imbalances between the Material Financial Control System and the CDB.

DFAS Cleveland corrected the posting logic that caused these errors to occur. Therefore, we are not making recommendations.

Journal Voucher Controls. Of the 61 out of balance JVs, 4 JVs, involving total debits of \$245 million and total credits of \$495 million, were recorded to correct errors that occurred because DFAS Cleveland accounting personnel improperly recorded JVs to the CDB before the DBMS trial balance was processed in September 2000. DFAS Cleveland calculated and recorded the four JVs to correct the CDB account balances.

Cost of Goods Sold Model. Of the 61 out of balance JVs, 2 one-sided JVs, valued at \$898 million, were recorded in the Cost of Goods Sold model to correct out of balance conditions in the Cost of Goods Sold trial balance. The out of balance condition occurred because DFAS Cleveland recorded prior period adjustments in CDB control accounts rather than subsidiary accounts. The Cost of Goods Sold model crosswalked the subsidiary account balance rather than the control account balance from the CDB trial balance to the Cost of Goods Sold trial balance. We are not making recommendations to modify the Cost of Goods Sold model because the Under Secretary of Defense (Comptroller) has not authorized changes to the model. Instead, the Under Secretary of Defense (Comptroller) is proposing a move to historical cost for valuation of inventory.

Supervisory Review and Approval of Journal Vouchers

The DFAS Cleveland, Director of Accounting, issued guidance for supervisory review and approval of JVs based on dollar value of the transaction.

Supervisory review is the principal internal control to ensure that the JVs are proper and supporting documentation is adequate. Review of 507 JVs indicated that 505 JVs (99.6 percent) were approved at the appropriate supervisory level in a timely manner. DFAS Cleveland substantially complied with the Director's policy. DFAS Cleveland's performance represents a significant improvement over prior years.

Summary

DFAS Cleveland had not yet completed its efforts to implement new accounting systems containing both proprietary and budgetary account structures or remedied the undistributed collection and disbursement problems in their

entirety. As a result, DFAS Cleveland was required to make entries at the departmental level that cannot be supported and subsequently create out of balance JVs which must then be recorded in order to correct system interface problems. Until field-level accounting systems are in compliance with financial regulations and field-level activities are brought into compliance with cash accountability standards, the majority of the unsupported and out of balance JVs recorded by DFAS Cleveland will continue to be made.

Recommendations, Management Comments, and Audit Response

Revised Recommendation. As a result of management comments, we revised draft recommendation A.1. to clarify actions necessary to improve management controls. We also added DFAS Columbus to the recommendation.

A.1. We recommend that the Directors, Defense Finance Accounting Service Charleston, Columbus, Norfolk, Oakland, and Pensacola comply with DFAS guidance for recording Centralized Expenditure and Reimbursement Processing System balances, both inception to date and current year balances, in the activity general ledgers and reconciling any differences.

DFAS Comments. DFAS partially concurred with the recommendation. DFAS stated that the DFAS field organizations currently follow DFAS Cleveland guidance requiring the field sites to adjust their monthly ledgers to match the Activity Control Ledger in the Centralized Expenditure and Reimbursement Processing System. DFAS indicated that the 19 JVs included in our report as unsupported were related to prior year balances for collections and disbursements. DFAS Cleveland is currently working on a cash rebuild project that will reinstate the correct starting balances for cash as of December 1994. The estimated completion date is scheduled for September 2001. See the Management Comments section for the complete text of DFAS comments.

Audit Response. We agree that 17 of the 19 JVs affected inception to date balances for Funds with Treasury. However, DFAS Cleveland was required to record the JVs to correct the inception to date balances because the DFAS field organizations did not record prior year Activity Control Ledger amounts in the Navy WCF activities general ledger accounts. For the remaining two JVs, DFAS Cleveland was required to record for current year collections and disbursements for the Navy Research Lab and Fleet Material Support Office because DFAS Charleston and DFAS Columbus did not record the Activity Control Ledger balances. Actions being taken, including the cash rebuild project, will satisfy the intent of the revised recommendation.

A.2. We recommend that the Directors, Defense Finance and Accounting Service Cleveland and Kansas City, reemphasize the requirement for departmental accounting and supervisory personnel to provide adequate supporting documentation for all journal vouchers.

DFAS Comments. DFAS concurred in principle with the recommendation and will emphasize the requirements for adequate supporting documentation shown in the DFAS guidance issued on October 5, 2000. DFAS did not agree with audit conclusions that seven JVs recorded in DDRS by DFAS Kansas City were not supported and provided comments on the supporting documentation for those JVs. DFAS indicated that five of the seven JVs were made as a result of and in accordance with action items from the Navy WCF Joint Review,⁶ which was attended by IG, DoD, personnel who did not object. DFAS provided specific comments on why it considered each of seven JVs as supported.

Audit Response. Actions taken by DFAS satisfied the intent of the recommendation. The seven unsupported JVs discussed in the IG report included three JVs to force the trial balance into agreement with budget execution reports and four JVs to correct identified errors.

The three JVs to force the trial balance into agreement with budget execution reports did not provide the level of documentation required by the DFAS guidance. Indicating that the need for the adjustment was discussed at the Navy WCF Joint Review does not by itself satisfy the documentation requirements. The supporting documentation should have included source data and the related analysis used to determine which is the correct amount, and documentation showing transactions reconciling the trial balance to budget execution reports. Forcing agreement of numbers from two different sources, even if required by DFAS or Under Secretary of Defense (Comptroller) policy, does not automatically constitute support for such a JV if the difference between the two numbers cannot be explained.

The four JVs to correct identified errors were not adequately supported because none of the JVs included a complete narrative discussion of the need for the adjustment, the source of data in the original entry and why the original entry was erroneous, or analysis documenting the correct amount and how that amount was determined. Indicating that the need for the adjustments was discussed at the Navy WCF Joint Review does not provide sufficient information about the need for the adjustment. The information provided in the DFAS response to the draft report far exceeded the narrative included in the JV.

⁶DFAS, Department of the Navy, Under Secretary of Defense (Comptroller), and IG, DoD, personnel have a joint meeting, usually in early December, to review an early draft of the financial statements to identify problems and actions that need to be taken to correct erroneous information or additional explanations that should be added to the footnotes to the financial statements. IG, DoD, personnel attendance at such meetings does not indicate automatic concurrence for action items or subsequent adjustments to the financial statements.

Finding B. Audit Trails

The audit trail from the ending trial balance in the CDB to the opening balances in the DDRS was not adequately documented. DFAS Cleveland accounting personnel adjusted the ending trial balance from the CDB to derive the opening trial balance in the DDRS and modified crosswalks from the CDB to the DDRS. Adjustments of \$5.9 billion were not recorded in the CDB but were needed for financial reporting purposes. However, documentation supporting the adjustments was not sufficient to permit tracing amounts from the source data within the CDB to amounts reported on the financial statements by DDRS. This occurred because the DFAS Director did not require DFAS Cleveland to directly post the CDB trial balance to the DDRS and record all subsequent adjustments in the DDRS. As a result, audit trails were not available to easily verify that the DFAS adjustments were consistently made.

Audit Trail Guidance

DoD Regulation 7000.14-R, volume 6, chapter 2, "Audit Trails," requires DFAS to ensure that complete and documented audit trails to source transactions are maintained to support reports it prepares. DoD Regulation 7000.14-R, volume 1, chapter 3, states that audit trails should allow a transaction to be traced from initiation through processing to final reports. A key test of the adequacy of an audit trail is whether tracing the transaction forward from the source or back from the result will permit verification of the amount recorded or reported.

Modification of Central Data Base Trial Balance

The intent of the DDRS was to provide a documented audit trail from source-level trial balance data to the general ledger values used to produce the financial statements. As part of the compilation process for the FY 2000 Navy Working Capital Fund Financial Statements, DFAS Cleveland accounting personnel were to provide trial balances from the CDB accounting system as input to the DDRS. Adjustments were to be documented and recorded in the DDRS for financial reporting purposes. Following the DDRS adjustments, the final DDRS trial balance was crosswalked to the various financial reports. In this way the integrity of the audit trail from the source to financial reports was to be maintained. However, DFAS Cleveland adjusted the ending trial balance from the CDB before importing the trial balance data into the DDRS. While the adjustments were needed, they were not adequately documented. The adjustments were needed because adjustments were recorded for financial reporting purposes at the end of FY 1999 that were not recorded in the CDB. In addition, adjustments were made to correct differences between control and subsidiary account balances.

Adjustments for Financial Reporting Purposes. As part of the preparation of the FY 2000 Navy Working Capital Fund Financial Statements, DFAS

Cleveland had to adjust the ending trial balance from the CDB because adjustments were recorded for financial reporting purposes at the end of FY 1999 that were not recorded in the CDB and other adjustments were needed for financial reporting at the end of FY 2000. The \$5.9 billion of adjustments, which impacted the financial statements but were not recorded in the CDB included:

- adjustments to restate accumulated operating results (these included adjustments to recognize the actuarial liability for workers compensation benefits and eliminating entries at the end of FY 1999), and
- adjustments to record assets and liabilities related to the afloat pre-positioning ships.

DFAS Cleveland also calculated the change during the accounting period for the 12 subsidiary accounts comprising Accumulated Operating Results (general ledger account No. 3310) and reclassified the amounts as Transfers In, Transfers Out and Other Financing Sources.

We were able to recreate the basis for these adjustments as a result of additional information provided during numerous discussions with DFAS Cleveland accounting personnel. However, DFAS Cleveland should have recorded the adjustments in the DDRS after the CDB trial balance was imported. In addition, DFAS Cleveland should establish a standard operating procedure that includes standard documentation for these types of adjustments.

Use of Control Account. DFAS Cleveland accounting personnel modified the crosswalk for Funds Balance with Treasury for the Component business area. Instead of using the subsidiary account balances, as prescribed by the crosswalk, accounting personnel used the control account balances (general ledger account No. 1010). The accounting personnel modified the crosswalk because transactions of \$43.6 million were recorded in the CDB to the control account instead of a subsidiary account. Recording transactions to the control account does not comply with DoD Regulation 7000.14-R. The adjustment should have been documented as a JV and recorded in the CDB at the end of FY 2000. However, the imbalance was not detected before the CDB accounting records were closed. DFAS Cleveland subsequently recorded a JV in CDB to correct the control – subsidiary account balances. Accordingly, we are not making further recommendations.

Budgetary Accounts. DFAS Cleveland did not sufficiently document the crosswalks used to convert budgetary accounts in the CDB to the USGSQL format used in the DDRS. As a result, we were not able to trace the budgetary account balances from the CDB trial balance to the opening balances in the DDRS.

Summary

The intent of the DDRS was to provide a documented audit trail from source-level trial balance data to the general ledger values used to produce the financial statements. However, because certain adjustments are recorded for financial reporting purposes only that are not recorded in the CDB, DFAS Cleveland modified the CDB data input to the DDRS. DFAS Cleveland personnel did not adequately document the modifications that occurred between the CDB trial balance and the opening balances input to the DDRS. In other instances, DFAS Cleveland accounting personnel modified the CDB trial balance for adjustments that should have been documented and recorded as JVs in either the CDB or the DDRS. Until standard operating procedures are established and standard documentation is developed, the audit trail from the CDB to the DDRS will not be adequate.

Recommendations, Management Comments, and Audit Response

B. We recommend that the Director, Defense Finance and Accounting Service Cleveland:

1. Import the Central Data Base trial balance to the Defense Departmental Reporting System without modification.

DFAS Comments. DFAS nonconcurred and stated that changes occurred after the CDB was closed that necessitated changes in the DDRS trial balance. In addition, an audit trail from the CDB ending trial balance to the DDRS beginning trial balance had been created using a spreadsheet application.

Audit Response. We disagree with the DFAS position. We believe that the offline spreadsheet could be used as supporting documentation for a JV recorded in DDRS. We were not able to validate the reliability of audit trails in the offline spreadsheet application that DFAS Cleveland used to prepare the FY 2000 financial statements because DFAS Cleveland did not provide the spreadsheets in a timely manner. The DDRS has a JV process that was created expressly for the purpose of allowing all JVs to be documented and subjected to internal control procedures. The use of an offline application to modify the CDB trial balance before it was imported to the DDRS defeated the internal controls envisioned by the JV process. We request that DFAS reconsider its position on the recommendation and provide comments on the final report.

2. Develop standard operating procedures and standard documentation to adjust accumulated operating results and record the journal voucher in the Defense Departmental Reporting System.

DFAS Comments. DFAS concurred that standard operating procedures and standard documentation were needed. The procedures and documentation to adjust the accumulated operating results should be in place by September 2001.

DFAS did not concur that the adjustments to accumulated operating results should be made via the formal JV process. DDRS beginning trial balance must coincide with the ending trial balance data from the prior period. Standard operating procedures and documentation will be maintained to provide an audit trail from the CDB to DDRS.

Audit Response. Management comments were partially responsive. We agree with the DFAS proposal that standard procedures and documentation for maintaining an offline spreadsheet be adopted by September 2001. However, we believe that the offline spreadsheet should be used as supporting documentation for a JV recorded in the DDRS. The DDRS included a JV module so that all adjustments made to the original trial balance data would be documented and subjected to internal control procedures. We do not believe there is a valid reason for not recording the adjustment within the DDRS. We agree that the beginning trial balance within DDRS should coincide with the ending trial balance from the prior period. If necessary, entries made for financial reporting purposes can be reversed at the beginning of the following accounting period within DDRS. We request that DFAS reconsider its position and provide comments on the final report.

3. Improve crosswalks and develop complete documentation used to populate budgetary information from other sources to the Defense Departmental Reporting System.

DFAS Comments. DFAS concurred and indicated that complete documentation and audit trails will be maintained and available by September 2001, for budgetary information found in DDRS.

Appendix A. Audit Process

Scope

We examined the processes and procedures used to prepare the Navy Working Capital Fund Financial Statements. Our review included an evaluation of procedures and controls over processes to consolidate and adjust financial data from Navy field organizations and other sources to prepare the FY 2000 Navy Working Capital Fund Financial Statements. The FY 2000 Navy Working Capital Fund Financial Statements reported total assets of \$25.1 billion, total liabilities \$6 billion, earned revenue of \$13.7 billion, and program costs of \$13.6 billion.

Limitations to Audit Scope. We did not examine the transactions supporting the financial data that Navy field organizations and other sources submitted. In addition, we did not evaluate the 173 JVs, valued at \$37.5 billion, that were recorded in DDRS to allocate intragovernmental transactions. Those JVs are discussed in IG, DoD, Report No. D-2001-139.

Audit of the FY 2000 Navy Working Capital Fund Financial Statements. We delegated the audit of the FY 2000 Navy Working Capital Fund Financial Statements to the Naval Audit Service. The Naval Audit Service disclaimed an opinion on the FY 2000 Navy Working Capital Fund Financial Statements, and we endorsed this disclaimer. The Naval Audit Service performed work at the Navy field organizations to reconcile financial data submitted by the organizations to DFAS and the subsidiary records at the organizations. We performed audit work on JVs recorded to financial data after receipt of the data into the CDB system.

DoD-Wide Corporate-Level Government Performance and Results Act Coverage. In response to the Government Performance and Results Act, the Secretary of Defense annually establishes DoD-wide corporate-level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following corporate-level goal, subordinate performance goal, and performance measures.

FY 2001 DoD Corporate-Level Goal 2: Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the Revolution in Military Affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-02)**

FY 2001 Subordinate Performance Goal 2.5: Improve DoD financial and information management. **(01-DoD-2.5)**

FY 2001 Performance Measure 2.5.1: Reduce the number of noncompliant accounting and finance systems. **(01-DoD-2.5.1.)**

FY 2001 Performance Measure 2.5.2: Achieve unqualified opinions on financial statements. (01-DoD-2.5.2.).

DoD Functional Area Reform Goals. Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objective and goal.

Financial Management Area. Objective: Strengthen internal controls. **Goal:** Improve compliance with the Federal Managers' Financial Integrity Act. (FM-5.3)

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in the DoD. This report provides coverage of the Defense Financial Management high-risk area.

Methodology

We reviewed the process that DFAS Cleveland used to record, consolidate, and summarize financial information from Navy field-level organizations and other sources.

We reviewed the procedures and management controls over JVs and accounting entries recorded by DFAS Cleveland, DFAS Kansas City, and the Naval Supply Systems Command. DFAS Cleveland recorded 672 JVs, valued at \$185.2 billion, in the CDB that affected the FY 2000 Navy Working Capital Fund Financial Statements. We reviewed 378 of the 672 JVs. We limited our review to JVs in excess of \$100 million that were recorded during the period October 1999 through August 2000 and all JVs recorded during September 2000. We also reviewed 24 JVs, valued at \$721.4 billion, that DFAS Cleveland recorded in the Cost of Goods Sold model at fiscal year's end. In addition, we reviewed all of the 105 JVs that DFAS Cleveland and DFAS Kansas City recorded in the DDRS.

Use of Computer-Processed Data. DFAS Cleveland used the CDB to consolidate and summarize financial information recorded in various field-level systems. We did not evaluate the financial information reported to the CDB, nor did we evaluate the general or application controls over the CDB. We concluded that the data were sufficiently reliable to meet the audit objective. Not evaluating the controls did not affect the results of the audit.

Audit Type, Period, and Standards. We performed this financial related audit from August 2000 through April 2001 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. We did our work in accordance with generally accepted Government auditing standards except that we were unable to obtain an opinion on our system of quality control. The most recent external quality control review was withdrawn on March 15, 2001, and we will undergo a new review.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD. Further details are available upon request.

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of the management controls.

Scope of Review of the Management Control Program. We reviewed the adequacy of DFAS Cleveland and DFAS Kansas City management controls over the posting and approving JVs in the CDB and DDRS for the preparation of the FY 2000 Navy Working Capital Fund Financial Statements. We did not assess management's self-evaluation of those controls.

Adequacy of Management Controls. We identified a material management control weaknesses as defined by DoD Instruction 5010.40 in the overall compilation process related to recording JVs. We did not consider the problems specifically discussed in this report to be material management control weaknesses. However, the overall compilation procedures, which include JVs to force buyer-side data to agree with seller-side data could not be supported; and the inability of DFAS Cleveland to reconcile these differences is considered to be a material management control weakness. Discussion of JV procedures and the processes for accounting for intragovernmental transactions are discussed in IG, DoD, Report No. D-2001-139.

Prior Coverage

As part of our audit coverage of the FY 2000 Navy Working Capital Fund Financial Statements, we issued the following reports:

- Inspector General, DoD, D-2001-139 "Compiling and Reporting FY 2000 Navy Working Capital Fund Intragovernmental Transactions," June 18, 2001
- Inspector General, DoD, Report No. D-2001-108 "Recognition of Revenues and Expenses in the Defense Business Management System," April 27, 2001

- Inspector General, DoD, Report No. D-2001-057 “Inspector General, DoD, Oversight of the Naval Audit Service Audit of the FY 2000 Navy Working Capital Fund Financial Statements,” February 21, 2001
- Inspector General, DoD, Report No. D-2001-022 “Inventory Revaluation for the Navy Working Capital Fund by the Naval Supply Systems Command,” December 18, 2000

The General Accounting Office and the Inspector General, DoD, have conducted multiple reviews related to financial statement issues. General Accounting Office reports can be accessed on the Internet at <http://www.gao.gov>. Inspector General, DoD, reports can be accessed on the Internet at <http://www.dodig.osd.mil/audit/reports>.

Appendix B. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Finance and Accounting Service
Director, Defense Finance and Accounting Service, Cleveland
Director, Defense Finance and Accounting Service, Kansas City

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations

Senate Subcommittee on Defense, Committee on Appropriations

Senate Committee on Armed Services

Senate Committee on Governmental Affairs

House Committee on Appropriations

House Subcommittee on Defense, Committee on Appropriations

House Committee on Armed Services

House Committee on Government Reform

House Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations

House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform

House Subcommittee on Technology and Procurement Policy, Committee on Government Reform

Defense Finance and Accounting Service Comments



DFAS-DAS

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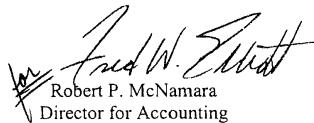


JUN - 8 2001

MEMORANDUM FOR DIRECTOR, FINANCE AND ACCOUNTING DIRECTORATE, OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on Compilation of the FY 2000 Navy Working Capital Fund
Financial Statements (Project No. D2000FC-0279.004)

Our response to the subject audit is attached. The point of contact is Mr. David
Arvin, (703) 607-2857 or DSN 327-2857.



Robert P. McNamara
Director for Accounting

Attachment:
As stated

cc:
DFAS-DDI
DFAS-AJIS/CL
DFAS-AX/KC

DFAS Comments on Audit Report on Compilation of the FY 2000 Navy Working Capital Fund Financial Statements (Project No. D2000FC-0279.004)

Responses to Recommendations.

Recommendation A.1. We recommend that the Directors, Defense Finance Accounting Service Charleston, Norfolk, Pensacola, and Oakland, reconcile differences between general ledger balances for Funds Collected (general ledger account No. 1011) and Funds Disbursed (general ledger account No. 1012) for the Navy Working Capital Fund organizations and the amounts shown in the Centralized Expenditure and Reimbursement Processing System.

Revised

Management Comments. Partially Concur. The DFAS field organizations at Charleston, Norfolk, Pensacola and Norfolk currently follow DFAS-Cleveland (DFAS-CL) guidance pertaining to the posting of year-to-date collections and disbursements. That guidance requires that the field sites adjust their monthly general ledger values when necessary, in order to match the Navy Working Capital Fund Activity Control Ledger (NWCFACL). The ACL is a byproduct of the Centralized Expenditure and Reimbursement Processing System (CERPS). It accumulates CERPS transactions to produce monthly, year-to-date (YTD) and inception-to-date (ITD) values of collections and disbursements for each activity. It should be noted that the Department of Defense standard general ledger accounts 1011 (collections) and 1012 (disbursements) are YTD accounts. The differences in YTD values are posted to unmatched collection/disbursement accounts at the field level and are included in the trial balance submitted to DFAS-CL. The same guidance requires the field organizations to reconcile between their general ledgers and the ACL. As a practical matter, primarily related to timing differences, this reconciliation is done after an adjusting journal voucher is posted.

DFAS-CL review of the 19 journal vouchers cited on page 6 of the report which support this recommendation shows that these departmental level entries relate to General Ledger Account Codes 1170 and 1180. These accounts carry the ITD values of collections and disbursements through the end of the prior fiscal year. In other words, the accounts are an accumulation of several years' worth of collections and disbursements. DFAS-CL is currently working on a cash rebuild project whose goal is to reinstate a correct starting cash balance for the NWCF activities as of December 1994, when the Defense Business Operations Fund was disestablished and the NWCF was established. Conclusion of this project should eliminate ITD differences from prior years.

The field organizations performed the cash reconciliations and the cash rebuild project will be completed by September 30, 2001.

Estimated Completion Date. September 30, 2001.

Recommendation A.2. We recommend that the Directors, Defense Finance and Accounting Service Cleveland and Kansas City, reemphasize the requirement for

departmental accounting and supervisory personnel to provide adequate supporting documentation for all journal vouchers.

Management Comments. Concur in Principle. DFAS Cleveland Accounting Special Project Office (DFAS-AAC/CL) memorandum dated October 5, 2000, Subject: Standard Operating Procedure (SOP) 7310.21, Journal Voucher (JV) Guidance, provided the requirements for adequate supporting documentation for all journal vouchers (attached). We agree to maintain emphasis on providing adequate supporting documentation for all journal vouchers (JVs). We disagree with the finding that the seven JVs recorded by DFAS-KC and referred to in the draft report were unsupported. However in relation to DFAS Kansas City (DFAS-KC), the recommendation is based on unsupported factual statements in the Audit Finding. We have placed emphasis on providing adequate supporting documentation for all JVs at DFAS Kansas City (DFAS-KC) for three years.

The DoDIG auditors reviewed 22 adjustments (JVs) made to Marine Corps Working Capital Fund (WCF) Audited Financial Statements (AFS) by DFAS-KC in the Defense Departmental Reporting System (DDRS). DFAS-KC mailed supporting documentation for all 22 JVs to DoDIG in Cleveland at its request. The DoDIG determined that seven of those 22 were unsupported. The DoDIG provided specific DDRS control numbers for the JVs at DFAS-KC's request. DFAS-KC reviewed the JVs and the documentation provided and do not agree that the documentation provided to the DoDIG for these seven JVs was insufficient. Five of the seven JVs were made as a result of and in accordance with action items from the Navy Working Capital Fund (NWCF) Joint Review. Representatives from the Office of Under Secretary of Defense (Comptroller), DoDIG, DFAS-CL, DFAS-KC, DFAS-Arlington and the United States Marine Corps attended the Review. Below are descriptions of the seven JVs organized by DDRS control number, who/what caused DFAS-KC to record the JVs, and the supporting documentation that was provided to the DoDIG.

DDRS 1239

DFAS-KC created a JV to record contributions for employee benefit and Voluntary Separation Incentive Program (VSIP) per data call and instructional guidance from DFAS-Arlington. DFAS-KC followed the guidance, but found the JV resulted in an out-of-balance condition between proprietary and budgetary general ledger balances. DFAS-KC created a second JV to reverse this erroneous JV. Upon further review of the field level trial balance, they found the benefit amount had been previously recorded in the Marine Corps subsidiary trial balance. They created an adjusting JV to correct the Government/Non-Government attribute in DDRS to match trading partner information per Department of Defense Financial Management Regulation (DoD FMR) Volume 6B, Chapter 13. The JV to reverse the data call item was deemed supported, however the JV to adjust the trading partner information (1239) was not.

DFAS-KC believes that both entries were supported given the same supporting documentation provided and consequently does not concur with this finding.

DFAS-KC provided the DFAS-Arlington created Employee Benefits spreadsheet from the DCPS query and JV instructions that applied to Depot Maintenance activity for these entries.

DDRS 2168 & 2170

DFAS-KC performed these two JVs as a result of the NWCF Joint Review. The Review discovered that the amount of NWCF activities disclosed on Note 21.A.2 (Available Borrowing and Contract Authority) did not reconcile to the NWCF Treasury Financial Management Service (FMS) 2108 report. DFAS-Arlington instructed DFAS-KC to accurately disclose this information. The requirement was also placed on the NWCF Joint Review action item list. DFAS-KC and DFAS-CL prepared a worksheet with activity level data based on the published FMS 2108 for consolidated NWCF AFS purposes. This spreadsheet, along with a hard copy of an email message from DFAS-CL point of contacts describing the adjustment, were provided as supporting documentation. DoDIG stated in its draft report that "no documentation was provided to show how the reconciliation was performed." The reconciliation of the FMS 2108 was attached with this JV to provide a more detailed analysis.

DFAS-KC does not concur with this finding since this entry was made as a result of the NWCF Joint Review. The DoDIG was in attendance and did not object to discussed action.

DDRS 2602

As a result of the Joint Review, a decision was made that all Transfers In and Out should be coded to the Non-Exchange attribute in DDRS. DFAS-KC originally followed the DoD FMR Chapter 13 guidance, but later performed an adjusting JV (#2183) to comply with the decision from the Joint Review. This adjustment (from Exchange to Non-Exchange) caused an out-of-balance condition on the Statement of Financing. DFAS-KC created an adjusting JV to correct the out-of-balance condition. The two JVs were attached together with the Joint Review action item listing. The second entry was perceived unsupported when both JVs had the same supporting documentation.

DFAS-KC does not concur with the DoDIG's finding because this JV was originally recorded correctly then adjusted to maintain consistent application within NWCF activities. Additionally, DoDIG representatives were present at the Joint Review and did not voice any objection to this matter when discussed extensively.

DDRS 2315

DFAS-KC performed this JV as a result of the Joint Review. This prior period adjustment was discovered to be recorded erroneously as a "Change in Accounting Standard." It should have been recorded to "Errors and Omissions in Prior Year Accounting Reports." DFAS-KC confirmed this finding and performed the adjustment per the Joint Review action item listing # 20. The action item list was attached as supporting documentation as well as a copy of the actual footnote for additional reference.

DFAS-KC does not concur with this finding, as this adjustment was necessary to disclose prior period adjustments accurately. Two items of supporting documentation were provided and this matter was discussed at the NWCF Joint Review to which the DoDIG did not voice any objection to this matter.

DDRS 2324

DFAS-KC completed the SF 133 for "Depot Maintenance, Other" without knowledge of critical closing guidance that existed only in an e-mail from 1998. This resulted in erroneous data in the September SF 133 and in the Statement of Budgetary Resources in DDRS. DFAS-CL adjusted the SF 133 to incorporate the closing guidance for consistent application for all NWCF activities. DFAS-KC made the required JV adjustment in DDRS to balance the Statement of Budgetary Resources to the adjusted SF 133 on file at DFAS-Sustaining Forces. The accurate SF 133 was included in the supporting documentation, as was the Statement of Budgetary Resources to show the affect of the JV given the relationship between the two reports.

DFAS-KC does not concur that this was an unsupported adjustment. It was made to reconcile inaccurate year-end budgetary information with the trial balance that was cross-walked to the AFS.

DDRS 2352

DFAS-KC performed this JV as a result of the Joint Review. Office of the Under Secretary of Defense (Comptroller) (OUSD(C)(AP)) discovered that a capital account related expense on the Statement of Net Cost was incorrectly crosswalked from the Defense Industrial Financial Management System trial balance for Depot Maintenance. It was erroneously crosswalked as "Not Attributable to Program." This amount was a surcharge transferred to reserve and was indeed attributable to a program. As a result of the Joint Review, OUSD(C)(AP) requested reclassification. DFAS-KC researched the activity and performed an adjustment reclassifying the amount to operating expense. The source trial balance, the Accounting Report (AR) 1307 and a description of the adjustment made were included for supporting documentation.

DFAS-KC does not concur that this was an unsupported adjustment, as the source document was included for support for this JV.

In conclusion, DFAS-KC does not concur with any of the DDRS-related JVs deemed unsupported by the DoDIG. In all cases source documentation was provided including descriptions of the JVs. Also, significantly all of these JVs were made as a result of action items from the NWCF Joint Review that the DoDIG attended. We are concerned that the DoDIG did not state objections during the Joint Review if they did not agree with decisions made between the participants. DFAS-KC is also concerned that this report states that there was no documentation or insufficient documentation for several JVs. DFAS-KC submitted supporting documentation for all JVs as requested.

Completion Date. October 5, 2000.

Recommendation B. We recommend that the Director, Defense Finance and Accounting Service Cleveland:

1. Import the Central Data Base trial balance to the Defense Departmental Reporting System without modification.

Management Comments. Nonconcur. The Central Data Base (CDB) System was closed for the fiscal year well before the required trial balance changes were known for the Defense Departmental Reporting System (DDRS). This necessitates changes to be made to the trial balance data in DDRS reporting system that cannot be included in the trial balance data from the CDB. Trial balance data changes from the CDB to DDRS, have a proper audit trail based on a spreadsheet application that tracks the ending trial balance data amounts in the CDB to the ending trial balance data amounts maintained in DDRS. Further difficulties arise in the next fiscal year when DDRS beginning balances must coincide with its ending balances from the preceding fiscal year that will not match the beginning balances maintained in CDB.

2. Develop standard operating procedures and standard documentation to adjust accumulated operating results and record the journal voucher in the Defense Departmental Reporting System.

Management Comments. Partially Concur. We concur that standard operating procedures and standard documentation should be in place. We do not concur that adjustments to accumulated operating results beginning balance should be recorded via the journal voucher process. DDRS beginning trial balance must coincide with its ending trial balance data. Standard operating procedures and documentation will be maintained to provide an audit trail from the CDB to DDRS.

Estimated Completion Date. September 30, 2001.

3. Improve crosswalks and develop complete documentation used to populate budgetary information from other sources to the Defense Departmental Reporting System.

Management Comments. Concur. We concur that complete documentation must be maintained that provides an audit trail for budgetary information utilized in DDRS.

Estimated Completion Date. September 30, 2001.

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

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